STATE OF MICHIGAN

IN THE SUPREME COURT

DAVID ABBO, an Individual,
COLORADO TOYZ, INC.,
a Colorado Corporation,
WIRELESS PHONES, LLC,
a Colorado Limited Liability Company,

Plaintiffs/Appellees,

vs.

WIRELESS TOYZ FRANCHISE, LLC,
A Michigan Limited Liability Company,
JOE BARBAT, an Individual,
RICHARD SIMTOB, an Individual,
JSB ENTERPRIZES, INC., a Michigan
Corporation, and JACK BARBAT,
an Individual,

Defendants/Appellants.

Supreme Court No. 149536
COA No. 304185
CC No. 2007-082804-CK
Hon. Shalina D. Kumar

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REPLY BRIEF IN SUPPORT OF APPLICATION FOR LEAVE TO APPEAL OR FOR PEREMPTORY REVERSAL

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REPLY BRIEF IN SUPPORT OF APPLICATION FOR LEAVE TO APPEAL OR FOR PEREMPTORY REVERSAL

ARGUMENT

Before turning to a detailed rebuttal of Abbo's brief in this Court, which is mostly concerned with matters peripheral at best to the issues before the Court, Wireless Toyz reminds the Court that this is a franchise case and that the offer and acceptance of franchise businesses in Michigan is heavily regulated by state (MFIL) and federal (FTC) law. The parties undertake to enter into a long-term contract-based relationship with detailed duties and responsibilities on both sides. The intention is that the documents will define when one party has breached the business agreement and what the range of consequences is.

The JNOV question presented here, in simplest terms, is whether a dissatisfied franchisee may allege a common law silent fraud claim based on oral statements allegedly made before the presentation of the UFOC—the statutorily required franchise offering document—when the franchisee has formally represented in writing that no such statements were made. (There are more reasons to reject the common law fraud claim in this case, including a valid merger/integration clause and a jury verdict against the franchisee on the MFIL §5 fraud claim for omissions and misrepresentations in the offer and sale of the franchises.)

The question arises: What more could the franchisor have done to prevent this later claim by the franchisee? Putting aside the question whether the alleged pre-offer statements were or were not made (for JNOV-review purposes, we must assume they were), the general legal issue is whether this sort of he said/she said credibility dispute can be eliminated as the basis of a *post hoc* challenge by any possible combination of documents prepared by the parties and their lawyers? If not, then it is now the law in Michigan that any subsequent agreement is voidable for fraud in the inducement, no matter what steps the parties take to prevent reliance on preliminary

oral conversations. More specifically, if a dissatisfied franchisee is willing to testify that a representative of Wireless Toyz at a Discovery Day reception inaccurately underestimated the historical impact of "hits" and "chargebacks"[1] on franchise profitability, that franchisee always will be able to later claim fraud, despite ignoring:

- the UFOC statement that earnings figures *exclude* operating expenses (Tab D at 43-46),[2]
- the UFOC explanation that all commissions are subject to chargebacks and that hits are discounts decided on by franchisees, based on local conditions and competition (*id.*),
- the Franchise Agreement's reiteration of these points (*e.g.*, Tab E §10.4 at 9),
- the franchisee's formal warranty in the Franchise Agreement that Wireless Toyz had *not* represented any specific level of costs,[3]
- the franchisee's signed Acknowledgment that *no* representation contradicting the UFOC or concerning operating expenses was made to him,[4]
- the franchisee's acknowledgment in the Development Agent Agreement that *no* representation was made as to costs or expenses except as set forth in the UFOC and that Wireless Toyz will not be bound by allegations of any such representations,[5] and

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1 "Hits" are cell phone discounts at the point of sale based on local competition, decided upon by franchisees. See §10.4 of Abbo's UFOC form agreement. "Chargebacks" are lost commission revenue when a customer's wireless service is cancelled within a carrier-specified period of time, typically 6 months. UFOC Item 6 disclosed that all commissions are subject to the chargeback contingency. Abbo admittedly understood both kinds of risks.

2 Tab D, the UFOC without attachments, is appended to Wireless Toyz' application for leave to appeal. The index to Tabs A through Q—the application attachments—is reproduced in the accompanying brief for the Court's convenience. Tabs R through V are attached to Wireless Toyz' supplemental brief.

3 Except as provided in the [UFOC] delivered to [Abbo], [Abbo] acknowledges that *Wireless Toyz has not*, either *orally* or in writing, *represented, estimated or projected any specified level of* sales, *costs* or profits *for this Franchise, nor represented the* sales, *costs* or profit level *of any other Wireless Toyz Store*. (Tab E §11.2 at 12; emphasis added)

4 Abbo represented that "[n]o oral, written or visual claim or representation, which contradicted the [UFOC], was made to me" (Tab F at (c)(2)) and that "[n]o oral, written or visual claim or representation except for what is included in the UFOC, which stated or suggested any sales, income, profit levels or *operating expenses* was made to me" (*id.* (c)(3)) (emphasis added).

5 *[N]either Wireless Toyz nor any of its agents* have *made* or are authorized to make *any oral*, written or visual *representations or projections of* potential earnings, sales, profits, *costs*,

- the merger/integration clauses in both the Franchise Agreement (Tab E §28) and the Development Agent Agreement (Tab G §16.9).

The circuit court, in granting JNOV, held that Wireless Toyz had done enough and that Abbo could not claim he was defrauded by statements about hits and chargebacks made on Discovery Day. The majority opinion in the court of appeals, essentially, has said that Abbo was free to ignore all the bullet-pointed items just listed and claim fraud anyway.

That is not the law elsewhere and should not be the law in Michigan, as Wireless Toyz has explained in the application (Application at 28-31, Supp Br at 11-12). *See Siemer v Quizno's Franchise Co, LLC*, 2008 WL 904874 at *7-8 (ND Ill, 2008) (Tab L); *Rocky Mtn Chocolate Factory, Inc v SDMS, Inc*, 2009 WL 579516 at *11-12 (D Colo, 2009) (Tab M); *Sherman v Ben & Jerry's Franchising, Inc*, 2009 WL 2462539 at *4-5 (D Vt, 2009) (Tab N); *Hardee's of Maumelle, Ark, Inc v Hardee's Food Systems, Inc*, 31 F3d 573, 576 (CA 7, 1994); *Joseph McSweeney Enterprises, LLC v Mister Softee Sales and Mfg, LLC*, 2013 WL 4588569 (D NJ, 2013 (Tab P); *Yogo Factory Franchising, Inc v Ying*, 2014 WL 1783146 (D NJ, 2014) (Tab V). Franchises are offered and sold nationally based on uniformly required disclosures. Although this Court has not decided a franchise case, Michigan law already supports Wireless Toyz' position. *E.g., Doty v CleanNet of Greater MI, Inc*, 2003 WL 22956401 at *3-4 (Mich App 2003) (Tab K); *Cook v Little Caesar Enterprises, Inc*, 210 F3d 653, 656-657 (CA 6, 2000) (applying Michigan law); *Aron Alan, LLC v Tanfran*, 240 Fed Appx 678, 682-684 (CA 6, 2007) (applying Michigan law) (Tab O).

Abbo's brief of appellees in this Court is notable for its detailed recitation of the evidence on claims the jury rejected and just as notable for its utter *silence* on document-based facts that

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expenses, prospects or changes of success *except as set forth in* [the UFOC] or as otherwise set forth in writing. (Tab G §1.4, last paragraph, at 3) (emphasis added)

are crucial to the silent fraud claim at issue here. Because the trial court granted a JNOV that set aside the silent fraud verdict, Abbo undoubtedly is entitled to have the evidence bearing on silent fraud viewed favorably to his claims. His brief, however, is cluttered with fact recitations unrelated to silent fraud. The basis for that claim is the allegation that misleadingly incomplete and inaccurate statements were made about hits and chargebacks in a pre-offer Discovery Day conversation. Abbo's evidence as to this July 2004 conversation was set forth in the application (Application at 11-12). Abbo insists that his failure to plead fraud in the inducement and his pre-verdict election not to seek rescission damages are no obstacle to upholding his verdict (the return of his original franchise fees), and the majority of the court of appeals panel agreed.

But the issue here does not concern all the matters that Abbo found to complain about during the years he operated his franchise, like the quality of Wireless Toyz' relationship with carriers, its training program, its advertising, the administration of the co-op program, etc.—matters that occupy pages of his brief. The issue is whether he was "tricked" into signing the Franchise Agreement and the Development Agent Agreement by oral statements made *before* delivery of the UFOC.

Abbo perseveres, however, in trying to justify the jury's verdict by claiming there was evidence that:

1. *Permitted the jury to find that Wireless Toyz could have compiled historical data from its franchisees about their past experience with hits and chargebacks and, thus, could have included that information in the UFOC* (*e.g.*, Abbo Brief at 8-9, 25);

Even if this were a finding that could be made on the evidence at trial, it is irrelevant without there being a duty to disclose information of this kind in the UFOC. Both Abbo and the panel majority found that duty in §5 of the MFIL, MCL 445.1505, the anti-fraud provision (Tab A at 9-10, 2014 WL 1978185 at *8). And in one sense that is exactly the right place to look for such a duty, along with §8 of the MFIL, MCL 445.1508, which sets forth in detail a franchisor's

disclosure obligations. But the jury found for Wireless Toyz on Abbo's §5 and §8 claims. Wireless Toyz already has explained why it had no duty to disclose information about hits and chargebacks and therefore cannot have committed silent fraud by not doing so (Application at 22, Supp Br at 4).

Moreover, the clear import of §34 is that civil liability cannot arise from a violation of §5, except as provided in the MFIL itself. Wireless Toyz has been couching this as a preemption argument (Application at 32-34, Supp Br at 7-9), but there is also another way to look at §34. The first sentence plainly states that "[e]xcept as explicitly provided in this act," there is no civil liability for violating any provision in the MFIL, including §5. The second sentence—the one Abbo claims proves there's no preemption (Abbo Brief at 38-39)—merely clarifies that other, preexisting liabilities are not *eliminated* by the MFIL. Abbo cannot find his "duty to speak" in the MFIL and then vindicate it outside the MFIL. That would be contrary to the first sentence. And even if there is not complete preemption and a common law silent fraud action is theoretically possible, which Wireless Toyz does not concede, the duty to speak must be found somewhere else, not in the MFIL. But both Abbo and the panel majority relied explicitly on §5 to create the duty that Wireless Toyz is alleged to have violated. Because there is no other source for the duty, JNOV was appropriately granted.

2. *Permitted the jury to find that the oral representations of Wireless Toyz' representatives were claimed by them to be derived from "information contained in the UFOC"* (*e.g.*, Abbo Brief at 6).

This is a puzzling claim, since as discussed next, Abbo's main contention about hits and chargebacks is that Wireless Toyz made a "deliberate decision" *not* to include this information in the UFOC. Abbo is apparently trying to connect the Discovery Day conversation about hits and chargebacks to the UFOC, realizing that his fraud claim should be based on the statutorily required formal offer made to him. In any event, this contention adds nothing to the actual claim.

The UFOC, like any written document, "speaks for itself." The existence of these operating expenses is disclosed, but not quantified, and offerees are advised to investigate the industry and check with past and existing franchisees to determine their effect.

The dollars-and-cents information actually contained in the UFOC is in Item 19. The Earnings Claims (Tab D, Item 19 at 43-46) lists the average results for 2003[6] in five categories—commissions per post-paid activation, post-paid activations per location, other activations per location, monthly store revenue from merchandise, and coop advertising credit paid per activation. The results are shown in a table (*id.* at 44), preceded by all-cap cautions (*id.* 43) and followed by notes A through L (*id.* 44-46). The first five notes explain what these categories represent. The table is preceded by a statement that the earnings claims do not reflect "the costs of revenues, operating expenses or other costs or expenses that must be deducted." In the notes that follow, note F again stresses that operating expenses and the cost of generating revenues are not reflected (*id.* 45).

3. *Permitted the jury to find that Wireless Toyz, knowing the importance of information concerning hits and chargebacks, "made a deliberate decision" not to include this information in the UFOC* (*e.g.*, Abbo Brief at 8, 24, 26).

Directly contrary to the previous point, Abbo points out the obvious—Wireless Toyz intentionally did not include statistics on hits and chargebacks in the UFOC. This, of course, was uncontroverted. The fact of this decision is explicit in the UFOC, Item 19, and elsewhere in the documents. But it is irrelevant in the absence of a duty to speak. Wireless Toyz had sound, nonfraudulent reasons for not including this variable, franchisee-driven, outdated information in the UFOC, which the jury heard. Hits (discounts) are point-of-sale decisions made by each

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[6] Abbo made no attempt at trial to contest the accuracy of any of this 2003 data. In his brief, he refers to this data as the "2004 earnings claims" (*e.g.*, Abbo Brief at 7). He contrasted this data with evidence of his own results in 2005, 2006, and 2007 (*e.g.*, Abbo Brief at 9).

franchisee, based on local conditions and competition. Wireless Toyz made no recommendations to franchisees concerning such variable costs. Historical chargeback information also was liable to be incomplete and unreliable, because chargebacks could occur up to six months after activation of new accounts and are demographically variable. Commissions for activations late in 2003 were still subject to being charged back when the UFOC in this case was finalized in April 2004.

Section 8 of the MFIL told Wireless Toyz what should be disclosed in the UFOC. Historical data on hits and chargebacks is not a statutorily required disclosure. In general, operating costs do not lend themselves to dollars-and-cents disclosure in the way that revenue items (commissions per activation, activations per store, merchandise revenue, etc) do. Under the MFIL, Wireless Toyz did not have a duty to disclose what it knew or could have known concerning past costs for hits and chargebacks. Without a duty to speak on the subject, there can be no common law silent fraud, even if the MFIL does not preempt that fraud claim completely (which it does). JNOV was properly granted by the trial court and improperly overturned by the court of appeals majority.

The majority acknowledged that David Abbo was an "entrepreneur" (Tab A at 2; 2014 WL 1978185 at *1). The dissent added, as the record bears out, that he had "proven business acumen" (Tab B at 4; 2014 WL 1978185 at *17). Abbo and his partner Michael Bober had an accountant working on their behalf as they were considering this franchise opportunity (*id.*). "This was not a case of parties with unequal bargaining power or plaintiffs with an exploitable susceptibility" (*id.*). Wireless Toyz points this out, not because it is necessary to support the JNOV granted here (the absence of a duty suffices), but to allay any concern that the JNOV is a harsh result. Abbo knew what it meant to agree that no oral representations were made to him

concerning costs and expenses if they were not to be found in the UFOC. He knew that the burden was on him to examine the UFOC closely and to learn by inquiry how operating expenses and the costs of generating revenues were affecting the profits of other franchisees. He had the names and contact information for all present and past franchisees. He said he contacted them. As this Court has said, "[i]gnoring information that contradicts a misrepresentation is considerably different than failing to affirmatively and actively investigate a representation." *Titan Ins Co v Hyten*, 491 Mich 547, 555 n.4 (2012).

This is not a matter of whether Abbo's claimed reliance was "reasonable" or not. He wants to frame the issue that way to suggest that Wireless Toyz' arguments are foreclosed by this Court's decision in *Titan*, 491 Mich at 557 (reliance not foreclosed because fraud was "easily ascertainable"). This is a matter of whether Abbo relied *at all* on anything he was told on Discovery Day, or whether that claimed reliance is a mere afterthought arrived at years later, in consultation with his lawyers about the prospects of suing Wireless Toyz. Abbo will protest that that is a question of fact resolved in his favor by the jury, but it is not a fact open to dispute in this case *because Abbo himself eliminated any possible reliance* when he signed the Franchise Agreement, the Development Agent Agreement, and his Acknowledgment, in all of which he avows that there were no oral representations made concerning expenses like hits and chargebacks. He was sophisticated enough and well-advised enough to know perfectly well what he was doing when he signed these documents.

It is telling that *nowhere* in the 40-page brief Abbo submitted to this Court does he so much as mention—much less deal with—his signed disclaimers of the existence of the very representations his claim is premised upon. He is silent because he has no answer to his own representations. Wireless Toyz did not sign the franchise agreements until after Abbo had signed.

Abbo dismisses the merger and integration clauses by claiming that they apply only to "agreements," not mere representations, but he forgets that *he* made representations too, and in writing. As discussed in Wireless Toyz' supplemental brief (Supp Br at 6-7), this Court enforces *all* the terms of unambiguous contracts, without weighing their wisdom. *Rory v Continental Ins Co*, 473 Mich 457, 468-70 (2005); *Bloomfield Estates Improvement Ass'n, Inc v City of Birmingham*, 479 Mich 206, 214 (2007); *McDonald v Farm Bureau Ins Co*, 480 Mich 191, 200-01 (2008); *DeFrain v State Farm Mut Auto Ins Co*, 491 Mich 359, 376 (2012). Abbo cannot use a silent fraud claim to defeat his contract by contradicting his own representations made in the contract.

The public policy of this state, as reflected in its franchise law, is to manage the business risks and rewards inherent in the franchise arena by requiring that offers be made in accordance with the MFIL's detailed disclosure obligations under §8 and broad anti-fraud provisions under §5. Abbo has no claim that Wireless Toyz did not comply fully with the MFIL. Abbo has lost his claim that Wireless Toyz committed fraud under the MFIL. That should be the end of it. Abbo's common law silent fraud claim was duplicative of and preempted by the statutory fraud claims the jury rejected (Application at 32-34, Supp Br at 7-9). The jury likewise resolved Abbo's contract claims, which under the economic loss doctrine, *Neibarger v Universal Cooperatives, Inc*, 439 Mich 512 (1992), means that Abbo simply has no other claim to make.

CONCLUSION AND RELIEF REQUESTED

For the reasons stated in its application, and in its supplemental brief, and for the additional reasons stated here, Wireless Toyz asks this Court to grant peremptory relief under MCR 7.302(H)(1) and reverse for the reasons stated in the court of appeals dissenting opinion (Tab B) and reinstate the JNOV entered by the trial court (Tab H).

In the alternative, Wireless Toyz asks this Court to grant leave to appeal from the May 13, 2014 majority decision of the court of appeals (Tab A) to consider the important questions of Michigan franchise law presented but inadequately addressed by the majority.

Respectfully Submitted:

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